April 4, 1995

DOCKET NO. G-008/GR-93-1090

ORDER AFTER RECONSIDERATION

BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

Don Storm	Chair
Tom Burton	Commissioner
Joel Jacobs	Commissioner
Marshall Johnson	Commissioner
Dee Knaak	Commissioner

In the Matter of the Application of Minnegasco, a Division of Arkla, Inc. for Authority to Increase Its Rates for Natural Gas Service in the State of Minnesota

ISSUE DATE: April 4, 1995

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PROCEDURAL HISTORY

On October 24, 1994, the Commission issued its FINDINGS OF FACT, CONCLUSIONS OF LAW, AND ORDER in the above-captioned matter.

On October 28, 1994, Minnegasco (or the Company) filed a petition for reconsideration of the October 24, 1994, Order.

On October 28, 1994, the Department of Public Service (the Department) and the Residential Utilities Division of the Office of the Attorney General (RUD-OAG) requested a variance to Minn. Rules, part 7829.3000, subpart 4, which allows ten days to answer a petition for reconsideration. The parties wanted the deadline for answers to Minnegasco's petition to coincide with the deadline for answers to the last timely petition filed by any party. The Commission granted the variance to adjust the filing deadline to a date certain: answers would be accepted through November 21, 1994, if the last timely filed petition was filed on or before November 11, 1994; answers would be accepted through November 28, 1994, if the last timely filed petition was filed on or before November 14, 1994.

On November 14, 1994, the RUD-OAG filed a petition for reconsideration and clarification of the October 24, 1994, Order.

On November 28, 1994, responses were filed by the RUD-OAG, Minnegasco, the Department, and the Suburban Rate Authority (SRA).

On February 2, 1995, the matter came before the Commission for consideration.

FINDINGS AND CONCLUSIONS

I. THE PETITIONS FOR RECONSIDERATION

A. Minnegasco

Minnegasco asked the Commission to reconsider four issues from the October 24, 1994, rate case Order: modification of the settlement on manufactured gas plant (MGP) costs; imputation of revenues from Minnegasco's appliance business to compensate for the affiliate's use of the utility's good will; allocation of the cost of gas leak checks to the unregulated appliance sales and service business when no leak is found; the Commission's decision not to increase the residential customer charge to $6 per month.

B. RUD-OAG

The RUD-OAG asked reconsideration of the Commission's decision to modify the parties' settlement regarding MGP costs. The RUD-OAG asked that the Commission either cap recovery at the settlement amount of $4,210,000 per year or affirm the settlement terms.

The RUD-OAG also asked the Commission to clarify its October 24, 1994, Order by stating that the RUD-OAG neither supported nor opposed the proposals of the Company or the Department on the residential customer charge.

II. COMMISSION ACTION

A. Summary of Commission Action

The Commission has carefully considered the briefs submitted and the arguments of counsel. Having fully reviewed the issues raised, the Commission finds that the decisions from its October 24, 1994, Order should be affirmed.

The Commission will accept Minnegasco's recalculation of the adjustment for the costs of gas leak checks. The Commission will require Minnegasco to submit revised income statements and rate base schedules supporting its authorized revenue requirements.

The Commission will grant the RUD-OAG's request to clarify the October 24, 1994, Order regarding the RUD-OAG's position on the residential customer charge.

The Commission will discuss its reasoning on the major issues in turn.

B. Manufactured Gas Plant Clean-up Costs

1. The Rate Case Final Order

The Company originally sought to include in test year expenses $4,615,000 to clean up former manufactured gas plant sites in compliance with state and federal environmental protection statutes. The Company also proposed to establish a tracker account to record actual clean-up costs and to adjust rates annually to reflect actual costs.

The settlement granted annual rate recovery of $4,210,000 and eliminated the tracker account/annual rate adjustment proposal. It also required the Company to place any insurance recoveries in a deferred debit account without carrying charges for consideration in the next rate case.

The Commission modified the settlement to limit annual cost recovery to $2.105 million, but authorized deferred accounting treatment for expenses exceeding that amount. The Order explained the Commission's goal was to ensure full recovery of environmental clean-up costs while avoiding over-recovery.

The Company and the RUD-OAG requested reconsideration.

2. Minnegasco's and RUD-OAG's Petitions

The Company asked the Commission to increase the annual recovery amount, claiming by affidavit it had already spent $2.9 million on manufactured gas plant clean-up during the first nine months of 1994. The Company also asked for a carrying charge on deferred clean-up expenses, citing fairness concerns and an earlier Commission decision in which a carrying charge was granted.[1]

The RUD-OAG asked the Commission to adopt the settlement agreement or, in the alternative, to cap total recoverable clean-up expenses at the settlement amount. The RUD-OAG argued that a cap would function as an incentive to control costs and would limit ratepayers' exposure to potentially burdensome clean-up costs.

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[1] In the Matter of the Application of Peoples Natural Gas Company, a Division of UtiliCorp United, Inc. for Authority to Increase Its Rates for Natural Gas Service in the State of Minnesota, Docket No. G-011/GR-92-132, FINDINGS OF FACT, CONCLUSIONS OF LAW AND ORDER (February 22, 1993).

3. Commission Decision

a. The Company's Requests

The Commission cannot consider the affidavit filed by the Company alleging that actual 1994 clean-up costs were running close to projections. The record is closed. The other parties have not had and will not have a chance to cross-examine the affiant or to conduct discovery in regard to the facts alleged. The Commission must disregard the affidavit and base its decision on facts in the record.

Those facts compel the original Order's conclusion that the elusive nature of these costs, together with the Company's track record in estimating them, justify limiting test year expenses to $2.105 million and granting deferred accounting treatment to actual expenses exceeding that amount.

The Commission will deny the request for carrying charges on clean-up costs deferred to the next rate case, because it would be inequitable for carrying charges to accrue on deferred costs, but not on deferred credits. (Under the terms of the settlement, any third party contributions toward clean-up costs enter a deferred credit account without carrying charges.)

Furthermore, the Commission has generally not allowed carrying charges on deferred manufactured gas plant costs. The People's case cited by the Company is an exception, and the facts in that case were unusual. There the costs at issue included costs already incurred, which the Commission found should be deferred and examined for prudence and reasonableness in the next rate case. Lengthy deferral of incurred costs is not at issue here.

b. The RUD-OAG's Requests

The RUD-OAG urged the Commission to accept the settlement or to cap recoverable amounts, including deferrals, at the settlement amount. As explained above, the Commission continues to believe it should not accept the settlement. The record compels the conclusion that the settlement amount will in all likelihood be off the mark and lead to overrecovery. For rate structuring purposes, the Commission has much greater confidence in the $2.1 million reconsideration figure than the $4.2 million settlement amount.

At the same time, as the October 24 Order makes clear, the Company's manufactured gas plant clean-up costs have been notoriously difficult to predict. It is possible the costs will exceed the reconsideration amount, or even the settlement amount. To be fair, and to avoid discouraging environmental clean-up, those costs should be recoverable through deferred accounting treatment.

The RUD-OAG suggests a cap on recoverable expenses as an incentive to control costs. The Commission believes the inconvenience of deferred accounting, the absence of a carrying charge, and pre-recovery review for prudence and reasonableness are likely to discourage extravagance. The Commission sees no need to cap recoverable expenses to encourage cost control.

C. Gas Leak Checks

1. The Rate Case Final Order

The Commission's cost apportionment decisions from the MAC/Minnegasco complaint proceeding, Docket No. G-008/C-91-942[2], were incorporated into the rate case calculations. In accordance with the Commission's March 24, 1994, Order in the MAC/Minnegasco complaint docket, Minnegasco's rate case filing allocated the costs of responding to customer calls for gas leaks according to whether the leak was on Company equipment or customer equipment.

The parties differed, however, on how costs should be allocated where **no** gas leak was found. MAC believed that costs in that case should be apportioned in the same manner as costs in a gas leak situation. Minnegasco believed that calls where no gas leak is found should be charged to the regulated operation.

In the October 24, 1994, final rate case Order, the Commission adopted MAC's position on cost allocations for calls in which no gas leak is found: these costs were to be allocated in the same manner as costs of calls in which a gas leak is discovered. The Commission adopted MAC's proposed $158,000 adjustment for this reallocation of costs. Although the Commission noted that Minnegasco disagreed with MAC's calculations, the Commission also noted that Minnegasco had offered no alternative calculation. The Commission therefore ordered Minnegasco to submit a compliance filing showing its detailed calculation of the adjustment that would result from the Commission's gas leak allocation decision.

2. Minnegasco's Petition

In its November 28, 1994, reconsideration petition Minnegasco asked the Commission to find that the costs of responding to a gas leak call where no gas leak is found should be allocated solely to the regulated operation. Minnegasco argued that a call in which no leak is found is not related in any way to the appliance sales and service operation and should not be charged to it.

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[2] In the Matter of the Complaint of the Minnesota Alliance for Fair Competition Against Minnegasco, a Division of Arkla, Inc. Affirmed by the Court of Appeals decision of March 28, 1995, C5-94-1820, C7-94-1821.

Minnegasco argued that the regulated utility has a safety obligation to respond to gas leak calls and must therefore be allowed to recover its resulting costs. Minnegasco cited a Commission decision[3] in which the Commission found that the costs which Peoples Gas Utility incurred in responding to safety calls on customers' private farm-tap lines could be recovered by the utility. The Company also argued that Minn. Stat. § 216B.16, subd. 11 requires that all emergency response costs be recovered by the utility.

If the Commission continues to require allocation between the regulated and nonregulated entities for non-leak calls, Minnegasco suggested a different allocation and a different calculation. Minnegasco argued that allocation should be based on the proportion of nonregulated repairs resulting from the calls.

Minnegasco submitted its own calculation for the allocation based on the Commission's October 24, 1994, decision. Minnegasco cited three errors in MAC's previous calculations; the resulting correction would yield a reduction in revenue requirements of $137,000 instead of $158,000.

3. Commission Decision

Having carefully reviewed the arguments raised by Minnegasco upon reconsideration, the Commission finds that its October 24, 1994, decision regarding allocation of costs for non-leak gas checks must be affirmed.

The allocation method clarified in the Commission's October 24, 1994, Order is consistent with FCC accounting principles under which Minnegasco's fully allocated costing is conducted. Consistency with these principles is appropriate and necessary in Minnegasco's fact situation, in which both the regulated operation and the nonregulated appliance sales and service operation are responsible for emergency calls.

The Commission disagrees with Minnegasco's argument that safety issues associated with the gas leak checks require a revised allocation of costs. The regulated utility has the obligation to keep its gas distribution system safe. Safety considerations should not be affected by the utility's decision to enter into a nonregulated operation which is also responsible for emergency calls. The resulting cost allocations should also be independent from safety concerns.

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[3] In the Matter of a Request by Peoples Natural Gas Company to Establish a Tariff for Repairing and Replacing Farm-Tap Lines, Docket No. G-011/M-91-989, ORDER REJECTING PROPOSAL, ALLOWING SERVICE, AND REQUIRING FURTHER FILINGS (October 26, 1992).

The Commission responded to the same safety arguments in its July 28, 1994, ORDER GRANTING PARTICIPANT STATUS AND DENYING REQUESTS FOR RECONSIDERATION in the MAC/Minnegasco complaint docket:

> The Commission disagrees with Minnegasco's analysis. The Commission's cost allocation decision does not mean that safety concerns would be sacrificed or that emergency responses would not occur. The Commission's allocation decision is a cost recovery issue for Minnegasco, not a barrier to repair of gas leaks. Order at p. 7.

And at p. 8 of the same Order:

> The Commission is confident that allocation of all costs to the utility would not be necessary in order for Minnegasco to carry out its duty of ensuring emergency response.

In its July 28, 1994, MAC/Minnegasco decision, the Commission also found that its Peoples farm-tap cost recovery holding did not control the Minnegasco gas leak allocation question:

> In the farm-tap situation, customers who owned the farm-tap equipment might be deterred from keeping it under repair if Peoples did not undertake the duty (and costs) of repair. In the Minnegasco situation, customers will presumably continue to call either Minnegasco or the appliance operation to respond to emergency leaks, no matter how the response costs are eventually allocated. The public policy reasoning behind the farm-tap decision therefore does not apply to Minnegasco's emergency repair situation. Order at p. 7.

The Commission is not persuaded that Minn. Stat. § 216B.16, subd. 11 requires allocation of non-leak emergency call costs to the utility. The statute does not contemplate a utility competing with itself for gas emergency response business, as is the case with Minnegasco and its nonregulated appliance operation.

The Commission has reviewed Minnegasco's calculations of the adjustment for costs of non-leak emergency calls and finds that they are appropriate. MAC has not objected to the Company's revised calculations. The Commission will therefore adopt Minnegasco's figures, resulting in a $21,000 adjustment to Minnegasco's revenue requirement.

D. Good Will

1. The Rate Case Final Order

In the October 24, 1994, final Order, the Commission restated a finding it had made in the MAC/Minnegasco complaint docket[4]: the Commission has the authority to impute revenue to the utility for the affiliate's use of the utility's good will. The Commission found that imputation was necessary in this case for the setting of just and reasonable rates. Finally, the Commission adopted the reasoning of the Department and the Administrative Law Judge that a one percent good will value is supported in the record.

2. Minnegasco's Petition

In its petition for reconsideration Minnegasco stated that the law, regulatory theory, and the record evidence require reconsideration of the one percent revenue imputation.

The Company stated that the Commission lacks statutory authority to require compensation from Minnegasco's appliance business because good will is a shareholder asset. In support of this argument, Minnegasco cited the fact that the value of good will (considered as the price above book value) goes to shareholders upon sale. Also, promotional advertising costs are not charged to ratepayers under Minnesota law.

According to Minnegasco, compensating ratepayers for the value of good will is against the precepts of cost of service ratemaking. Ratepayers do not pay for good will, suffer a detriment or experience the removal of a benefit, nor has there been any dissipation of an asset.

Minnegasco argued that there is no record evidence to support the Commission's imputation of revenues for the value of good will to Minnegasco's appliance business. According to Minnegasco, the record is clear that good will holds no positive value for the nonregulated operation, given the associated regulatory costs. Minnegasco argued that the only record evidence of the specific value of Minnegasco's good will to the appliance business is the testimony of the Company's witness Mr. Slocum, who stated that the net value was negative.

3. Commission Decision

a. Introduction

At the February 2, 1995, meeting, Minnegasco noted that the Commission's rate case final Order answered three main questions under the heading of good will. First, does the Commission have the authority to impute revenue to the utility for the affiliate's use of the utility's good will? Second, if the Commission has the authority to impute, should it choose to do so in this case? Third, if the Commission determines that imputation is necessary to achieve just and reasonable rates, what is the value of good will?

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[4] This decision was affirmed by the Court of Appeals on March 28, 1995, C5-94-1820, C7-94-1821.

Minnegasco stated that the first question, the Commission's authority to impute revenue, is currently before the Minnesota Court of Appeals in the MAC/Minnegasco complaint docket appeal. The Company stated that the second question, the propriety of imputation in this case, is a question of Commission policy. Minnegasco confined its oral arguments to the third question, the valuation of good will.

For two reasons, the Commission will also confine its discussion of good will in this Order to the third issue. First, the Commission agrees with Minnegasco that the Commission's authority to impute will be addressed by the Minnesota Court of Appeals, and that the propriety of imputation in this case is a matter of Commission policy choice. Second, every argument currently raised on the first two issues has been exhaustively briefed, argued, considered, and answered in three previous Commission Orders: the Commission's
March 24, 1994, and July 28, 1994, MAC/Minnegasco decisions and the October 24, 1994, final rate case Order.

b. Summary of Commission Action

The Commission has carefully considered each argument raised in these reconsideration proceedings. The Commission has studied the written briefs, listened to the arguments of counsel, and reviewed its own prior decisions. Having given full consideration to these matters, the Commission finds that Minnegasco has raised absolutely no new issue or argument which requires reconsideration of the Commission's good will decisions.
Although the Commission will not be granting Minnegasco's request for reconsideration of the good will issues, the Commission will here provide a discussion of the valuation of good will. This issue was not reached in the MAC/Minnegasco complaint docket and has therefore only been addressed in the rate case final Order.

c. The Value of Good Will

The Commission disagrees with Minnegasco's conclusion that only its witness Mr. Slocum presented valid testimony regarding the value of good will. The Commission does not find Mr. Slocum's testimony regarding negative net value convincing, and does not agree that his testimony is the only evidence on record.

Minnegasco's witness Mr. Slocum netted good will value against associated regulatory allocated costs to arrive at a negative net value of good will to the appliance operation. In the rate case final Order the Commission found that a finding of negative value for good will goes against both logic and the record. The Commission quoted its March 24, 1994, Order in the MAC/Minnegasco complaint docket:

> In the Minnegasco case, both logic and the record indicate that a value flows to the nonregulated entity from Minnegasco's conduct of its regulated utility business. Minnegasco's long history of service and its widespread service coverage have made it "the gas company" in the minds of the public.
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> The record in this case also supports a finding of value in Minnegasco's name and good will. The East Metro Brand Marketing Test shows that Minnegasco's name can draw three times the customer inquiries to a new nonregulated venture than can an unrelated name. It is clear that the Minnegasco name brings value to the nonregulated entity.
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> October 24, 1994, Order at p. 24.

The Commission disagrees with Minnegasco's conclusory statement that the value of good will must be netted against the appliance operation's allocated costs to arrive at true value. The Commission is seeking the **value of the asset** which has been given to the nonregulated operation without compensation to the utility. As the Administrative Law Judge stated at p. 38 of his report,

> ...the Commission seeks to know the value of "good will" as defined, standing alone, and is not concerned herein with the fact that the business's use of the name "Minnegasco" brings with it other financial consequences (for example, cost allocations mandated in the MAC Complaint case that may diminish the overall value of the nonregulated appliance operations).

Minnegasco is essentially asking the Commission to consider the appliance operation's profitability when valuing good will. Such a consideration would not be useful because there are countless decision options and other variables contributing to an entity's profitability which are independent of the value of the utility's name. The Commission is concerned with a valuation of the utility's name, image, and reputation, not a valuation of the appliance operation, nor an analysis of the operation's efficiency or profitability.

The Commission also disagrees with Minnegasco's contention that Mr. Slocum's testimony is the only record evidence on good will value. The Department submitted the testimony of its witness Ms. Bender regarding valuation. Ms. Bender advocated valuing good will by the consequent increase of sales for the appliance operation. Ms. Bender recommended a conservative estimate of one percent of the nonregulated entity's gross revenues. MAC submitted evidence of a range of imputations from two percent to five percent in other jurisdictions.

The ALJ considered the testimony presented and recommended adoption of the Department's position. The Commission used its discretion, applied its technical expertise, and adopted the ALJ's finding. The Commission found the value of good will to the nonregulated operation to be one percent of gross revenues.

d. Conclusion

The Commission will not reconsider its finding regarding the value of good will to the nonregulated appliance sales and service operation. The Commission was unpersuaded by the reasoning and evidence presented by the Company's witness. The Commission carefully considered all written and oral testimony, and the ALJ's recommended findings regarding good will value. Having fully considered the evidence, the Commission adopted the Department's finding of a good will value based on one percent of the appliance operation's revenues. The Commission here reaffirms this decision.

E. Residential Customer Charge

1. The Rate Case Final Order

Originally, the Company proposed to raise the residential customer charge, the fixed monthly charge residential customers pay regardless of usage, to $6 per month. The Company explained that its class cost of service study placed the fixed costs of serving the average residential customer between $13 and $15 per month and that the increase proposed in this case was part of a long term strategy to align customer charges more closely with fixed costs. The proposed increase would amount to $2 for former Midwest Gas customers and $1 for other customers.

The Commission authorized a $1 increase for former Midwest Gas customers to equalize the customer charges of all Minnegasco customers, but rejected the rest of the proposal. The Order explained that heavy reliance on residential customer charges conflicts with important public policy goals by making rates less understandable and credible to residential customers and by undermining residential conservation incentives.

2. Minnegasco's Petition

The Company requested reconsideration, emphasizing that the rejected proposal had been unopposed and again presenting the case for higher residential customer charges.

3. Commission Decision

First, as the Suburban Rate Authority (SRA) points out, the proposal was opposed by members of the public who appeared at the public hearings and filed written comments with the Administrative Law Judge. It was also strongly criticized by the SRA, which focused more on developing rate design policy than on the increase at issue.

Furthermore, although the Commission does not frequently reject proposals that are unopposed, it has the authority and responsibility to do so when rejection serves the public interest. That was the case here. The Commission has carefully re-examined its customer charge decision and continues to believe it is correct for the reasons set forth in the original Order.

III. THE RUD-OAG'S REQUEST FOR CLARIFICATION OF ITS POSITION ON THE RESIDENTIAL CUSTOMER CHARGE

In the Commission's October 24, 1994, final rate case Order, the Commission stated that the RUD-OAG concurred with Minnegasco's proposed increase of the residential customer charge to $6 per month. The Order also stated that the RUD-OAG agreed with the Department's recommendation to require the Company to design and conduct a public education program explaining customer charges.

In its November 14, 1994, petition for reconsideration and clarification, the RUD-OAG asked the Commission to clarify the October 24, 1994, Order regarding the RUD-OAG's position on the customer charge. The RUD-OAG stated that it had not affirmatively agreed with either the Company's or the Department's proposal. According to the RUD-OAG, it simply chose not to dispute these recommendations. The RUD-OAG sought clarification of its position in order to avoid confusion regarding the RUD-OAG's viewpoint in future proceedings.

Upon reconsideration of this matter, the Commission agrees with the RUD-OAG that its position should be clarified. The Commission clarifies its October 24, 1994, Order by stating that the RUD-OAG neither supported nor opposed the Company's or the Department's proposal regarding the residential customer charge.

ORDER

1. The Commission adopts Minnegasco's calculation of the adjustment for costs of non-leak emergency calls, which will result in a $21,000 adjustment to Minnegasco's revenue requirement.

2. Within 30 days of the date of this Order Minnegasco shall submit revised income statements and rate base schedules supporting its authorized revenue requirement.

3. The Commission clarifies its October 24, 1994, Order by stating that the RUD-OAG neither supported nor opposed the Company's or the Department's proposal regarding the residential customer charge.

4. The Commission denies all other aspects of the requests for reconsideration. All requirements of the October 24, 1994, Order remain in force and effect.

5. This Order shall become effective immediately.

BY ORDER OF THE COMMISSION

Burl W. Haar
Executive Secretary

(S E A L)